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COTTAGE SITE SUBCOMMITTEE MEETING OCTOBER 1, 1998 1:00 PM FOURTH FLOOR TRAINING ROOM JOE R. WILLIAMS BUILDING BOISE, ID

Cottage Site Subcommittee members:

State Controller J.D. Williams, Chairman
Superintendent of Public Instruction Anne C. Fox
Secretary of State Pete T. Cenarrusa

Chairman Williams called the meeting to order at 1:15 p.m. He explained that this meeting was originally planned as a session to review recent cottage site sample appraisals with all the affected leaseholders and to start finalizing rental rates, but the lessee organizations have requested more time to look at the appraisals. Chairman Williams announced that department staff would brief the subcommittee on the appraisals today and this briefing session would be open for questions and observations.

Stan Hamilton, Director, Idaho Department of Lands, said that some questions may have to be deferred to the appraisers since department staff did not do these appraisals. He introduced in-house appraiser Alvin Carr, Lands Leasing Specialist, who would provide information on the appraisals.

Review of Priest Lake Preliminary Appraisal Report

Mr. Carr said the Priest Lake appraisal contract was awarded to Mr. John McFaddin on June 2, 1998. Mr. McFaddin's preliminary report was received by the department on August 13 and forwarded to Mr. Doug Cresswell, Priest Lake Lessee Association President, on August 14. Following review, department staff provided written comments to Mr. McFaddin on September 9 and he responded to those comments on September 15. The lessees' consulting appraiser, Mr. Ed Morse, provided his written comments to Mr. McFaddin September 15 and Mr. McFaddin responded to Mr. Morse's comments September 21. The department met with Mr. McFaddin and the lessees' representatives on September 16. The department completed final review of the preliminary appraisal report and comments received on September 28.

The highest and best use for the cottage sites is single recreational home site. The Priest Lake and Payette Lake contracts instructed appraisers to appraise parcels at fee simple value and recommend market rent for the cottage sites.

Mr. Carr identified the subject lots that were appraised. These are the same lots that were selected randomly for the 1991-92 appraisal. The appraiser compared sales information of more than 100 current sales and listings to the subject properties. In his analysis of market rent, the appraiser identified 3.5% which he then applied to the unimproved market value of the subject properties to arrive at a conclusion of market rent value. The appraiser applied the improved value of a number of leased lots along the west side of Priest Lake, forest service lots, and comparable recreational sites over to the subject property deducting lessees improvements such as sewer, water development, electrical services and access, to arrive at unimproved lot value. This was a comparable sales appraisal.

Bryce Taylor, Chief, Bureau of Range Management & Surface Leasing, noted that there has been an active market on Priest Lake the past three or four years in fee simple sales. Mr. Taylor said the appraiser considered using the income approach or the replacement approach, but found the comparable sales approach to be preferable for dealing with fee simple lots. The appraiser compared what's occurred in the private sector and in the leasing market and then made those comparisons to the state lots.

Mr. Carr said the appraiser was instructed to determine fee simple value considering the lot as though vacant and unimproved, so there was no need for him to consider the consequences of lessee improvements.

Chairman Williams asked how market rent fit into the equation. Mr. Carr explained that market rent would be determined by researching the rental rates of similar properties and by using market rates of return. The appraiser researched available data that indicated there was not adequate information for a comparable private lease type rate and went into the market analysis using a percentage of fee simple value.

Mr. Taylor said the appraiser found some private leases on Lake Pend Oreille that he felt were similar. Forest Service rates on the other side of Priest Lake are not really comparable and were not used for justification. The appraisal also reports what some other states are doing. Mr. Taylor said the department feels enough comparables were used.

Dr. Fox noted a wide variation in the values of Lots #6 and #275. Mr. Carr acknowledged that there is a dramatic difference in that Lot #6 at Outlet Bay has no road access, shallow water, not much beach, and it is fairly narrow. Lot #275 at Huckleberry Bay has better access and beach frontage. Mr. Taylor said that the last two or three times the department has examined property values at Priest Lake, they have specifically identified boat access only versus drive-in access. Previous appraisers have said that drive-in access creates a 75% differential. The department has spent improvement funds building roads at Priest Lake anticipating generating some good income for the beneficiaries. Access improvements will elevate those land values and the beneficiaries should be able to recoup some of that investment in rental income. Dr. Fox asked whether roads could be built to Lot #6. Mr. Carr replied that roads could be built, but at substantial cost. Priest Lake Area staff has looked and has not found a convenient location for an access road.

Chairman Williams asked if market rent was determined just as a percentage of fee simple value. Mr. Taylor answered that it was. The appraiser recommended that market rent should be a percentage return of the fee simple value and suggested 3.5% after he examined what other market evidence he could find. Mr. Hamilton said the appraiser's instructions did not specify that rental be expressed as a percentage of asset value, they just simply asked him to identify what a reasonable rental would be in each case and he chose to express it as a percentage of value.

Mr. Cenarrusa asked about the determination of unimproved value. Mr. Carr responded that the appraiser applied comparable sales to the subject, then deducted for the amenities, to arrive at vacant unimproved as per the instructions. Mr. Taylor added, as an example, that the appraiser went to the three or four local sewer districts asking them what it would cost to hook up to them today and also asked some contractors and some lessees what it would cost to put in a septic system. From that information the appraiser deduced the cost would be about \$6,000 per lot.

Dr. Fox pointed out that the 3.5% rental rate used on the Summary of Conclusions comes from the Montana study. She asked whether the appraiser knew that the board had voted for 2.5%. Mr. Carr said the appraiser was well aware of the history of the state lease program and rental rate formulas. The 2.5% rate reflected low end to consider some of the lessees' sweat equity and improvements, but Mr. McFaddin looked at the market and identified those lessee improvements from the improved value and deducted that and went to the market analysis and came up with 3.5% for the unimproved value. Mr. Taylor added that the 3.5% didn't come just from the Montana appraisal. The private leases on Pend Oreille are in the very same market and the appraiser identified that was probably the most reliable information for the Priest Lake market.

Chairman Williams asked if the fact that these are state leases was taken into account. Mr. Taylor said there were no discounts for that. The appraisal instructions were to look at the lots for fee simple value and determine anticipated rent. Mr. Carr emphasized that the appraiser did consider lease provisions as per instructions on the market rent. The analysis also considered the values received by lessees through lease assignments and included several different approaches to arrive at a conclusion of 3.5%. This analysis of market data was consistent with several sources.

Dr. Fox asked whether there were any appraisals that department staff had questioned. Mr. Hamilton commented that the department had had several appraisals of properties over the years along the shoreline of Priest Lake, including a number of fee MAI appraisals. Mr. Carr responded that staff had not seen anything in these appraisal figures that was inconsistent with past appraisals. Mr. Taylor said that of the fifteen lots appraised, eleven ended up being higher than the county assessed value and four ended up being lower, which is not a drastic difference.

Chairman Williams asked what the process would be now to take this data from the fifteen lots and apply it to all the other lots. Mr. Carr said staff would need direction from the subcommittee before proceeding. Mr. Taylor explained that the department would assemble a team with Alvin Carr as the team leader. The Real Estate Bureau has another appraiser in Coeur d'Alene who would help. Three staff people in the Priest Lake Area who are infinitely familiar with the roads and have all worked with the cottage sites over the years would also help. The team would walk the accesses out and look at the beach and see what the lessees have done. Going from the

appraisal, they would apply the same kind of dollars to the improvement credit. Mr. Taylor anticipated this process would be very intensive, requiring a couple of weeks on site and then putting some numbers together.

Chairman Williams said the deadline for having it all done is June 30 of next year. Mr. Taylor said the department's deadline would actually have to be much ahead of that. Mr. Hamilton emphasized that the full board should review the appraisal and provide direction before the department moves ahead.

Charles Lempesis, attorney for the Priest Lake Lessee Association, commented on behalf of the lessees. He reported that the lessees do not feel the appraisals are complete because the associations have not provided their comments. Chairman Williams assured him that the subcommittee was just being briefed at today's meeting and the lessees would be given an opportunity another day to present their view.

Review of Payette Lake Preliminary Appraisal Report

Mr. Carr began the briefing on the Payette Lake Cottage Sites appraisal by noting that the appraisal contract was awarded to Mr. Bradford Knipe of Knipe & Knipe on June 17. The department received a preliminary appraisal report from Mr. Knipe on August 31. A copy of the preliminary appraisal report was forwarded to Mr. Charles Hervey, Payette Lakes Lessees Association, on September 1 and to Mr. Richard Smith, Pilgrim Cove Lessee Association, on September 8. The department has just recently reviewed the preliminary report and provided written comments to the appraiser as of September 30. A meeting with the appraiser, the lessee representative, and department staff is scheduled for next Thursday, October 8, to look at comments relative to the appraisal report and any additional information. As at Priest Lake, the appraiser was to identify the fee simple value as though vacant and unimproved subject to any outstanding rights and reservations of record. Again, market rent would be identified by researching the rental rate for similar property and by using market rates of return and requiring the appraiser to do good research and consideration of market rent. The appraiser was instructed to look at the highest and best use for the cottage site, single recreation residential home site, and to consider any other factors deemed relevant to the appraiser in the evaluation process. As at Priest Lake, provisions of the state lease were to be considered and the appraiser was to analyze the lease in reporting the value of market rent. In both cases the state lease was considered in market rent analysis.

Mr. Carr said the department has abided by the instructions for the appraisal contract and will be meeting with the appraiser and the lessee representatives. Staff has provided any information presented to the department by the lessees to the appraiser in its entirety for consideration in the preliminary appraisal report. The department is asking for comments from the lessee association for the appraiser's review in anticipation of a final report in an adequate time frame to meet the land board's desires. The appraisal report that Mr. Brad Knipe provided was the appraisal of fourteen lots at Payette Lake, seven lakefront and seven non-lakefront.

Mr. Carr reviewed the Summary Appraisal Report. The appraiser considered the McCall residential market in his analysis and then a summary of fifty-two assembled sales that he considered under the market rent analysis. He looked at ten comparables with some additional information from six additional sources. He looked at the sales data as though unimproved and applied unimproved value over to the subject properties. Then he identified a market rent based

on 6% of fee simple. The appraiser went into some depth on the market rent analysis and canvassed market rent nationally.

Chairman Williams asked Mr. Carr to explain the difference between market value and the value of single legal home site. He noted that, in one case, the appraiser came up with a value of \$250,000 for a lot the county assessed at \$234,000 for 1998. Mr. Carr said that particular lot is on the very north end of the lake. The appraiser describes that if the lot were not occupied, it likely could not be occupied because it would not fit within zoning ordinances. It was built before zoning hit the local area. The vacant lot value would be \$170,000. Because it is built on and serving its purpose as a single home site, the appraiser deemed it worth \$250,000.

Dr. Fox asked where the improved market value, backing out the lessee improvements, is addressed in this appraisal. Mr. Carr explained that it is not shown on the Summary Appraisal Report because that analysis and adjustment was made to the comparable. Mr. Knipe deducted the improvement value from the comparable rather than the subject property. It is a different approach than Mr. McFaddin used, but the result is essentially the same.

Chairman Williams noted that the appraiser's value for the lakefront lots is generally higher than the county assessor's appraised value. For non-lakefront lots, just the opposite is generally true; the appraiser's value is less than the county appraisal, with one exception.

Mr. Taylor acknowledged that the average county assessed value or market value at Payette Lake was 93% of the appraised value. The next-to-last column on the Value Table shows the assessed value over the market value ratio. He pointed out that, like the state, the county uses older data than the appraiser uses. The appraiser was looking at very current data. That would explain some differences between his values and the county values.

Dr. Fox asked what the suggested 6% rental rate was based on. Mr. Carr answered that the appraiser had concluded that 7% or more may be more appropriate, but he recommended just 6%. Mr. Hamilton said the department has done a number of appraisals of properties for exchange in this area plus the assessor has been at work for several years valuing properties on a formal basis. The appraisal of these lots is fairly consistent with the history.

Chairman Williams asked about the difference between the appraiser's recommendation for Priest Lake at 3.5% and the appraiser's recommendation for Payette Lake at 6%. Mr. Taylor felt that question should be deferred to the appraisers. Mr. Hamilton recalled that there was some discussion in the Priest Lake review supporting the 3.5% rate considering the rate of appreciation that had been occurring in that area.

Chairman Williams asked if anyone had any comments about the Priest Lake appraisal.

Mr. Lempesis responded that it was not appropriate yet to comment on the appraisal except in the context of the process. He said it would be more appropriate for an appraiser to comment on the lessee's view of the appraisal, but Ed Morse could not be present today. Mr. Lempesis listed some of the lessees' concerns. First, according to the appraisal instructions, it was clearly agreed and the subject of some negotiation, the state had to do the appraisal. The appraisal instructions say that the lessees are to have no contact with the appraisers. The state would contract and monitor and coordinate the appraisal. Mr. Lempesis said that all the comments made by the staff about the preliminary report seem to have been accepted by the

subcommittee as being conclusionary or final, but the lessees do not accept it as final. The process to which the lessees agreed in writing was that prior to the final report being issued, they would have an opportunity to comment. The 16th of September was the only time this issue has been addressed from the lessees' viewpoint. Mr. Lempesis said he sent a letter to Bryce Taylor in May recommending a discussion during the appraisal process. He proposed to have the appraiser meet with the lessees to hear their concerns. In August, a letter was sent to Alvin Carr asking about the process, but no response to that letter has been received. On August 28 Mr. Lempesis received the appraisal and wrote to express his concern that it was not clearly denoted as a preliminary appraisal by virtue of the fact that neither the lessees association nor the lessees themselves had provided any input. The lessees need to be involved in the process in the manner originally agreed. Mr. Lempesis said that the full land board would receive the appraisals at the November 4 regular land board meeting, but that both sides must look at the appraisal and communicate to the subcommittee what the strengths and weaknesses of the appraisal may be before it goes to the full board.

Mr. Lempesis also expressed concern that the subcommittee has not concluded the appeal process. He said that issue should be addressed now before the appraisal issue is resolved.

Mr. Taylor said that a meeting with the Payette Lake Lessee Association and the appraiser is scheduled October 8. The deadline to receive final comments from Priest Lake is October 9. When department staff met with the lessees in Priest Lake, Mr. Lempesis indicated to Mr. Taylor that for all of the lessees to be able to respond they need to know the values on their lots. That can't be done until the extrapolation is done, as a matter of practicality. Mr. Taylor said the preliminary appraisal has been addressed as such by the department. There has not been an attempt to finalize it today. Staff has met with the association and taken their verbal and written comments and the appraiser has responded to those. A final conclusion on the appraisal needs to be reached so that the extrapolation can be done and then department staff can meet with the group of lessees. When they know what their lot value is, they can have more meaningful input.

Chairman Williams asked Mr. Lempesis if Ed Morse had given written comments. Mr. Lempesis said Mr. Morse has not yet prepared written comments, but he has prepared questions to Mr. McFaddin both orally and in writing to which Mr. McFaddin has responded.

Chairman Williams asked how much time the lessees need to prepare to present to the board. Mr. Lempesis hesitated to respond for Mr. Morse, but said he expects the work could be completed during October.

Mr. Lempesis said he didn't disagree that extrapolations have to be done, but expressed concern that the extrapolations might be based upon this preliminary appraisal. He used as an example credits given for improvements such as docks. For this appraisal, a smoothing factor was done for docks saying a dock is worth \$2,500, but docks are substantially greater in value than \$2,500. He said it would have been beneficial for Mr. McFaddin to have information and data that makes the process more credible before arriving at some of these conclusions.

Mr. Taylor commented that almost all of the lessees whose lots were appraised happened to be on site. Some information was passed on to the appraiser at that time, not in every case but certainly in some. Mr. Cresswell said that the lessees were not notified of the appraisal and very few of the lessees were on site at the time of the appraisal of their lots. Mr. Carr said in the

process of administering the contract, department staff notified all of the subject lots being appraised with a copy of the appraisal instructions and have passed on any information received from the lessees group from the time the contract was let. Information the lessees indicated was pertinent was provided, through the department, to the appraiser.

Chairman Williams said it's necessary for the lessees to have input for a reasonable period, maybe five or six weeks. He asked Mr. Greener if waiting until mid-November to hold a final meeting would be adequate. Mr. Greener said he shared the concerns stated by Mr. Lempesis. He said the lessees are not prepared to have a meaningful conference on October 8. He said he would like to talk with Mr. Hervey and Mr. Lempesis before setting a date for that meeting. He noted that Payette Lake is about three or four weeks behind Priest Lake in the appraisal process.

Mr. Lempesis reviewed several items that need to be done including the extrapolation, the subcommittee's approval of the appraisal, the board's approval of the appraisal, meetings with the lessees, finishing up the legal technicalities of the appeal process, and dealing with the hardship issues that were left until the appraisal came in. He suggested listing these items on a calendar and working backward to get some deadlines.

Mr. Hamilton said Mr. Lempesis' goal of having the land board approve rates in March is probably realistic. Staff believes the board must deal with the appraisal issue sooner because the extrapolations can't be done without having the appraisal approved.

Chairman Williams said the preliminary decision needs to be made this year. At his suggestion, the subcommittee agreed to review the appraisals in November and take the issue to the full board in December.

Mr. Carr brought up another issue. The letter that was sent for the October 9 meeting was based on the board's desire to finalize the rental by the November board meeting. If information was sent to the department by October 9, Mr. McFaddin could have a final report in by October 19. The appraiser and staff will meet October 8, then wait for comments, but could not have a report from Mr. Knipe until November 13. Mr. Knipe is doing a cottage site appraisal for the BLM in Montana for three weeks beginning October 9.

Mr. Williams said that the subcommittee's goal is to be ready to approve the appraisals at the regular meeting in December. Dr. Fox asked whether, if the baseline data comes in, the department could start the extrapolations on the other lots before the weather becomes a problem. Mr. Carr responded that staff could not make that effort without direction from the subcommittee and the board.

Mr. Taylor suggested that if the lessees concur, staff could begin on the baseline data on the provision that if something is adjusted the baseline data could be adjusted. Staff could get some measurements of access and look at some beach frontages. The field work could be started now and the office work could be done later.

Chairman Williams said the October 8 meeting would be deferred until the first week of November.

Mr. Lempesis asked if the Priest Lake lessees' final written comments for the appraiser's review

could be due at the same time as Payette Lakes, October 31.

Mr. Greener said Alvin Carr had mentioned a summary prepared by the department of the preliminary appraisal at Payette Lakes which he had not received yet. Mr. Carr explained that the Summary for Priest Lake is the first part of the Priest Lake Appraisal Report and the Payette Lake summary is just the letter of transmittal, contents, and market analysis taken from the Payette Lake Appraisal.

Mr. Cresswell said he hadn't received the staff's review and written comments. Mr. Taylor explained that those had been sent to the appraiser for corrections and would be provided for the lessees.

Mr. Cresswell commented that the appraisal instructions indicated that the lessees would be credited for their improvements, they would be backed out entirely, plus limitations. The appraiser didn't value the improvements as highly as the lessees think they should be. Mr. Cresswell will give the department more information on this. Also, he said the appraiser didn't make any adjustments whatever for limitations in the leases. The lessees feel their leases are more limiting than most rental contracts would be. That needs to be taken into consideration. Mr. Cresswell said the market rent study that has been done is not adequate. The appraiser should look at Priest Lake rather than Montana and Minnesota.

Dr. Forney said that the appraisal of his lot is severely faulted and the appraiser never contacted him. He shared a summary of things he would like to have considered. The first two pages of Mr. Knipe's appraisal show pictures taken of the beach May 9 when the lake was down. That section of the beach is underwater in summer. Dr. Forney said that what the appraiser referred to as his lot's "protected swimming area" is actually his neighbor's property. His lot was appraised at \$750,000 as raw land. Mr. Taylor pointed out that Dr. Forney's lot was appraised for exchange, not for rental. Perry Whittaker, Real Estate Bureau Chief, said that the appraiser has reanalyzed Dr. Forney's lot and revised his numbers to \$600,000.

Chairman Williams asked about timing on the exchange. Mr. Whittaker said that the briefing meeting for the exchange is November 16.

Mr. Williams suggested that if a lessee thinks the appraisal for his lot is too high, the lessee should get an independent appraisal. Dr. Forney agreed that would be fair.

Ben Ysursa asked about the discrepancy between the county assessed value and the appraisal of Dr. Forney's lot. The county only appraised it as one home site, but there are two homes on the lot. Dr. Forney said even though there are now two homes on his site it should be considered as one home site. The lot is long and narrow and it is encumbered in the middle by a sewer station. The older existing home could not be rebuilt because of these restrictions. Mr. Knipe considered the lot as a large piece of property that could be divided into four units.

Mr. Dewayne Bills questioned the methodology of the Payette Lakes appraisal. He said an accurate answer was never given to Dr. Fox's questions about market value, unimproved market value, and the offset for improvements. He said staff glossed over the issue of what is really the cost of the raw land as opposed to market value. Mr. Bills is a professional builder and subdivider and is currently subdividing properties in the Canyon County area. He said the average cost of unimproved ground in relationship to the finished lot price with all improvements

is about 20%. The tendency on the part of the appraiser, which, he said, is absorbed by staff, is to think that improvements are only 20% of market value so the cost of the raw land must be 80%. Mr. Bills leased his lot in 1972. He said at that time it was a raw piece of ground with a narrow dirt road. He had to put in a better road, water, sewer, and other amenities to turn the raw land into a homesite. Mr. Bills stated it would be unfair for him to pay 80% of the raw land value and only get 20% credit for the actual improvements that he has put in. He concluded that the ratios have been turned upside down and the issue of bare land has not been addressed.

Dr. Fox suggested using the same type of format for the Payette Lakes and Priest Lake appraisal reports so that the actual value of the improvements is identified and deducted on both. Mr. Taylor said that could be discussed with Mr. Knipe.

Dr. Fox asked how all the variations people have mentioned, such as the difficulty of building on bedrock, can be taken into consideration. Mr. Hamilton explained that those would be identified in the extrapolation process. The agreed-upon values in the appraisal will be used as comparables and each lot will be compared back to a reasonable comparable and a series of adjustments will be made for each lot.

John Corbeil said that lessees should be able to talk to the appraisers. The state intends to have all of the lessees approach and get access to their leased land from a road. He said the state cut his lot in two behind the garage less than twenty feet and made a bank on one side. He said it's very difficult to have access and it's going to cost him a lot of money to figure out some way to get in. He said the state had told him he could buy a right-of-way across his neighbor's lot but, he said, it would cost \$12,500 to cut down trees and pay for dirt to be brought in. The bank is too sharp to get his car, boat trailer, and camper through, anyway. He said he should be able to point these problems out to the appraiser.

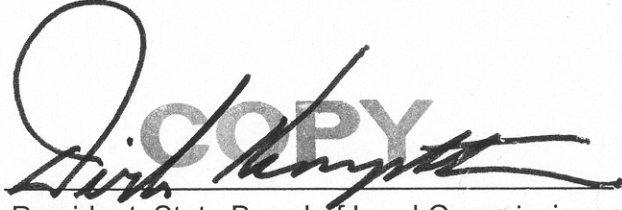
James T. Anderson asked if the appraisers actually tried to find year-round rentals for comparables and if those were used in determining fair market rent. Mr. Taylor answered that they had looked for those and the appraisal reports show which realtors they checked with. The appraisers did not find any bare land lot rentals on Priest Lake or at Payette. Mr. Taylor added that 6% is one suggestion, it is not what the board is considering.

Jack Flaherty noted that the Priest Lake appraisal came in recommending 3.5% and Payette Lake, 6%. He said a recommendation is an opinion and the appraisers are way off.

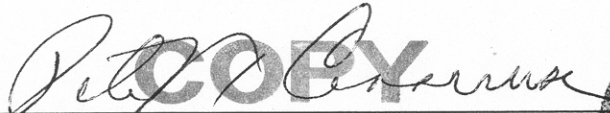
Mr. Hamilton requested a copy of the materials Dr. Forney provided for the record.

Chairman Williams adjourned the meeting and thanked everyone for attending.

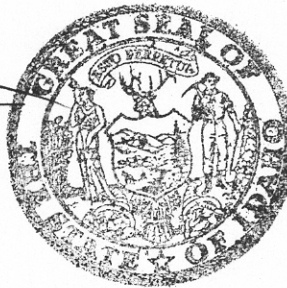
IDAHO STATE BOARD OF LAND COMMISSIONERS



President, State Board of Land Commissioners and
Governor of the State of Idaho



Pete T. Cenarrusa
Secretary of State





Stanley F. Hamilton
Director